

STATE OF IOWA  
DEPARTMENT OF COMMERCE  
UTILITIES BOARD

IN RE:  QWEST COMMUNICATIONS INTERNATIONAL INC. SALE OF PUBLISHING BUSINESS	DOCKET NO. SPU-02-15
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**ORDER FINDING JURISDICTION**

(Issued September 4, 2002)

**PROCEDURAL HISTORY**

On August 20, 2002, Qwest Communications International Inc. (QCII) announced an agreement to sell its QwestDex directory publishing business to a nonaffiliated entity. QCII's press release regarding the sale implies a belief on the part of QCII that regulatory approval of the proposed transaction is not required in Iowa. However, based on the limited information available to the Utilities Board (Board) at the time of the press release, it appeared to the Board that regulatory review may be required in Iowa before the transaction may be closed.

In order to determine the scope of its jurisdiction regarding this matter, the Board issued an order in this docket on August 21, 2002, directing that on or before August 28, 2002, Qwest Corporation (Qwest) file an application for approval of the proposed reorganization, a request for a waiver of the review requirement, or a detailed explanation of the basis for Qwest's apparent belief that review is not required in Iowa. The Board emphasized that any claim that Board review is not

required must specifically address the issue of imputation of directory publishing revenues and the effect of that issue on the proposed transaction.<sup>1</sup> Other interested parties, including the Consumer Advocate Division of the Department of Justice (Consumer Advocate), were invited to file comments at the same time regarding the application of Iowa Code §§ 476.76-.77 (2001) to these circumstances. Finally, the Board noted that time is of the essence in this matter and stated that if a proposal for reorganization were filed, the Board intended to bring this matter to a conclusion as soon as possible, rather than taking the full time allowed by statute.

Timely filings were made by Consumer Advocate, the Carlyle Group and Welsh, Carson, Anderson & Stowe (collectively, the Buyers), and Qwest Corporation (Qwest), the public utility subsidiary of QCI that offers regulated local exchange service in Iowa.

### **SUMMARY OF COMMENTS**

Consumer Advocate's response argues that the proposed transaction is subject to Board review pursuant to Iowa Code §§ 476.76-.77. Consumer Advocate notes that § 476.76 defines a "reorganization" to include "[t]he sale . . ., directly or

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<sup>1</sup> The Board notes that at least one other state regulatory agency has concluded that issues associated with imputation of directory publishing revenues required investigation and resolution, see "Order Granting Joint Motion To Reopen The Record, Approve Stipulation And Agreement For Continuation Of Directory Imputation, And To Waive Response Time," issued August 20, 2002, by the Public Utilities Commission of Colorado as Decision No. C02-899. In that order, the Commission approved a stipulation among Qwest, Commission staff, and the Office of Consumer Counsel that re-states Qwest's imputation obligations while providing for the possible sale of QCI's directory publishing assets. As a result, the Commission was able to avoid setting the proposed transaction for hearing.

indirectly, of the whole or any substantial part of a public utility's assets." This definition is qualified with the words "unless the context otherwise requires." Section 476.72 defines "public utility" to include "only . . . rate-regulated telephone utilities providing local exchange telecommunications service." This definition is also qualified with the words "unless the context otherwise requires."

Consumer Advocate notes that when a carrier such as Qwest is regulated pursuant to a price regulation plan approved by the Board under § 476.97, Consumer Advocate is required to report to the General Assembly on an annual basis the estimated return earned by Qwest as if it were subject to rate-of-return regulation, and specifically requires that this calculation be made in two ways, one taking into account the investment, revenues, and expenses associated with the sale of classified directory advertising and one omitting that information.

Consumer Advocate then describes the history of imputation of directory publishing revenues in Iowa, noting that Qwest has admitted that a certain amount of the revenues from directory publishing continue to be embedded in Qwest's current prices for local telephone service, even though Qwest is operating under a price regulation plan.

Consumer Advocate argues that the reorganization review statute is a statute that regulates conduct for the public good and should therefore be liberally construed in favor of the public interest, citing McCracken v. Iowa Dept. of Human Services, 595 N.W.2d 779, 784 (Iowa 1999) and other cases. Based on all of this, Consumer

Advocate concludes that QCII's directory publishing business is closely and immediately related to Qwest's public utility business and the implications of the proposed transaction for ratepayers and the public interest, including its effect on imputation and future pricing of local telephone service, require Board review of the transaction before it may be closed.

Finally, Consumer Advocate argues that Qwest's financial plight is no reason to try to accelerate the Board's review process in this docket and that any procedural schedule should allow adequate time for discovery, an informed opportunity for the parties to develop their positions, and meaningful settlement discussions.

The Buyers assert that the Board lacks jurisdiction over the proposed transaction because the assets are not "public utility assets" as defined in the statute. They also argue that the proposed transaction will be good for QCII, for Qwest, for the customers of Qwest, for the customers of QwestDex, and for the public generally, as it will strengthen QCII's financial position and provide additional resources to QwestDex to support development of innovative new products and services.

The Buyers do not directly address the imputation issues raised in the Board's order, but they argue that the Board has a long-standing view that rate issues are not appropriate for consideration in the reorganization review process. The Buyers cite a variety of past Board orders in support of this principle, including In re: GTE Midwest Incorporated and Iowa Telecommunications Services, Inc., "Order Terminating Docket, Etc.," Docket No. SPU-99-29 (April 23, 2000). The Buyers argue that under

this precedent, imputation issues should not be considered in the present docket and should be left to any future proceedings in which Qwest might propose to modify its price regulation plan or otherwise raise the issue.

Qwest's response starts with a more detailed description of the proposed transaction and includes partial copies of some of the agreements relating to the sale.<sup>2</sup> Qwest takes the position that the Board does not have disapproval authority over the Dex sale because Dex is not a "public utility" and the assets being sold are not "public utility assets" as defined in the relevant statutes. As far as the imputation issue is concerned, Qwest argues that it is operating under a price regulation plan that includes imputation of directory revenues in rates for basic communications services and the proposed transaction will not change Qwest's rates. Qwest further states that it does not intend to initiate any request to change rates as a result of the Dex sale or "any changes to current imputation, during the term of the price plan." (Qwest Response at page 4.)

### **BOARD JURISDICTION**

The Board finds that it has jurisdiction to review the proposed transaction pursuant to Iowa Code § 476.77 and that, in the absence of a waiver issued pursuant

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<sup>2</sup> The Board refers to the agreements as "partial copies" because they do not include at least one side letter, disclosure agreements, and other ancillary documents that are referred to in the sales agreements and represent material parts of the transaction agreement and because at least one of the agreements, identified as Exhibit C or the "Dexter Agreement," is missing at least one page.

to § 476.77(4), the transaction cannot take place until the Board's review is completed.

The Board understands the position of the Buyers and Qwest that QwestDex, itself, is not a public utility asset. But, even if correct, that is not the end of the inquiry.

First, the Board agrees with Consumer Advocate that §§ 476.76-.77 are remedial statutes intended to protect the public interest and should therefore be interpreted in a manner that will fulfill the legislative intent. The Legislature clearly intended that the Board's jurisdiction should be interpreted in this manner, as demonstrated by the broad definition of "reorganization" to include the "acquisition, sale, lease, **or any other disposition, directly or indirectly**, including by merger or consolidation, of the whole or any substantial part of a public utility's assets." (Emphasis added.) By this language, "any" "indirect" disposition of a public utility asset is a "reorganization." The statute could hardly be broader in its scope.

"Public utility assets" is not a defined term in either the reorganization statute or rules. The Board concludes the public utility assets that are being disposed of in the proposed transaction, as presently structured, are the revenues generated by QwestDex and imputed to Qwest's Iowa local service revenue requirement. In Qwest's most recent rate review proceeding (Docket No. RPU-93-9), the Board imputed Yellow Pages revenues in the amount of approximately \$17.9 million per year. Based on that figure, which may understate the current value of Yellow Pages

revenues, the imputed revenue reduces Qwest's local service bills by as much as \$1.50 per month per customer. By any measure, the imputed revenue stream is an asset that has substantial value to the public utility and its customers. Approximately 17 years of corporate restructuring efforts to divorce directory publishing profits from the local exchange service business and to put that money into shareholders' pockets rather than ratepayers' pockets have not succeeded. Those profits continue to benefit the local exchange service portion of QCII.

The proposed transaction, however, threatens the continued viability of imputation of directory revenues. It is appropriate to impute revenues from a Qwest affiliate to Qwest as a public utility, but it may be difficult to continue to impute revenues if the directory publishing company is no longer an affiliate. To the extent the sale of QwestDex could make imputation impossible in the future, the sale is an indirect disposition of the public utility asset of imputed revenues.

This does not mean that a full-blown reorganization review proceeding is required in this docket. It is still possible that Qwest could make the case review is unnecessary and seek a waiver of that review, pursuant to § 476.77(4). The Board may grant a waiver where review is not necessary in the public interest. In balancing the public interest in granting a waiver, the Board recognizes the following items would tend to weigh in favor of waiver:

1. A binding assurance from Qwest that in any future rate proceeding of any nature, it will be precluded from arguing against imputation

on the grounds that the directory publishing business has been sold. Qwest could reserve any other arguments it may have against imputation, as well as the opportunity to suggest appropriate methods for calculating imputed revenues in a future rate proceeding.

The Board understands Qwest's argument that imputation is a moot issue so long as Qwest operates under a price regulation plan, but the Board is also aware that Qwest's current plan has a remaining term of only a little over two years. Qwest's commitment that it "does not intend to initiate any request to change rates as a result of the Dex sale, not any changes to current imputation, during the term of the price plan" (Qwest Response at page 4) is insufficient because it is only a statement of present intent, rather than a commitment, and it is, at best, of only two years' duration. That is not sufficient to satisfy the Board that review of the proposed transaction is not necessary in the public interest.

2. Specific assurance from Qwest that sufficient capital will continue to be invested in Iowa to maintain service quality that meets or exceeds all requirements in Board rules and the Qwest/U S West settlement.

3. It appears that this QwestDex sale may well be part of a series of asset sales that could include another attempt to sell Qwest's rural exchanges. The structure of the bidding process in Qwest's earlier attempt to sell rural exchanges made it nearly impossible for Iowa interests to make a bid for only

the Iowa exchanges. The structure of the bidding process may have eliminated potential bidders with a proven track record of providing excellent service to rural Iowa. Board review after a future sale agreement is reached is too late to prevent recurrence of a bidding process that may not be in the public interest for Iowa customers. The public interest would be served by a Qwest assurance that bidding in any future sale of Iowa rural exchanges will be structured to allow bids for only Iowa exchanges.

4. Perhaps the most important issue in whether Board review of the QwestDex sale is not necessary in the public interest is the effect on the financial stability of Qwest caused by the delay inherent in review. Any request for waiver must address this issue.

Finally, it is necessary to address the Buyers' argument that Board precedent establishes that rate-related issues are not appropriately considered in a reorganization context. The Buyers are correct that the Board has consistently found that rate case issues should be considered in future rate case proceedings, if necessary, but in each case where the Board has applied that principle it has been clear that the issue would still be viable and capable of resolution in those future proceedings. This case is different. If the QwestDex assets are sold without reasonable assurances along the lines of those described above, then the imputation issue may effectively become moot before the Board can consider it. Thus, in the prior cases the Board reserved ratemaking issues to future rate cases; here, the

Board must preserve the issue or it may be decided by default. This is a significant difference.

Based upon its current understanding of the facts and circumstances, the Board finds that the proposed sale of QwestDex by QCII is an indirect disposition of substantial public utility assets of Qwest and the proposed sale cannot take place without the Board's prior review pursuant to Iowa Code § 476.77 or a waiver pursuant to § 476.77(4).

#### **ORDERING CLAUSE**

##### **IT IS THEREFORE ORDERED:**

Qwest is directed to file a proposal for reorganization regarding the proposed sale of QwestDex or a request for a waiver of that review before the proposed sale is closed to allow for Board review of the proposal or request.

#### **UTILITIES BOARD**

/s/ Diane Munns

/s/ Mark O. Lambert

ATTEST:

/s/ Judi K. Cooper  
Executive Secretary

/s/ Elliott Smith

Dated at Des Moines, Iowa, this 4<sup>th</sup> day of September, 2002.